



Roger.Whidden@us.pm.com on 10/19/2001 01:10:49 PM

To: Jeffrey Richman/Atty/DC/ArnoldAndPorter@APORTER
cc:

Subject: FW: LeBow unbowed

Jeff:

Following up on our recent conversation, here's some information that may be relevant to your analysis. Please call me when you're ready to schedule a call to discuss your preliminary conclusions. Thanks.

Roger

> -----Original Message-----

> From: Lenling, Amy > Sent: Friday, October 19, 2001 12:22 PM
> To: Whidden, Roger; Desel, Paula; Suter, Eric; Osborne, Kevin (PMMC
> Legal); Nelson, Christopher (PMMC); Carcich, Claire; Murillo, Joe;
> Murphy, Virginia; Holleran, Jack; Keane, Denise
> Subject: LeBow unbowed
> > Below is an article from today's Miami Daily Business Review on Vector
> Tobacco Group's plans to market Omni, which will be available in two
> weeks. Bennett LeBow states "It [Omni] may open us to legal liability - I
> don't care. I tell my people I don't want to hear that." LeBow said that
> he dismissed attempts by his lawyers to discuss the legal ramifications of
> creating a truly safe cigarette. The article also contains quotes from
> Philip Morris on the genetically modified tobacco used by Vector.
> > The article also focuses on Vector's planned marketing of the product.
> Omni's \$75 million to \$100 million marketing campaign's slogan is "premium
> Taste, Less Carcinogens." > > "They can still give you emphysema and heart trouble,"
LeBow says. "But
> we're working on that. We think we can fix that." > > LeBow unbowed > > Miami
Daily Business Review
> 10/19/01
> Lynda Edwards
> > It's the Holy Grail for smokers: a luscious, safe cigarette. And in two
> weeks, Omni, the "safe" cigarette of Miami-based Vector Group, parent of
> Liggett Tobacco Co., will hit the shelves, culminating a 30-year process
> costing more than \$100 million. > > Vector is rushing to patent a process that
treats tobacco with palladium,
> used in car catalytic converters, to reduce carcinogens. According to
> Vector studies, the palladium process reduces some Omni carcinogens by 15
> percent to 60 percent. In a second step, Vector is planning to launch Omni
> Nicotine Free, a cigarette made of a genetically modified tobacco, early
> next year. > > Eventually, Omni Nicotine Free will include the palladium process. >
> This is the first time Bennett LeBow, the chairman and chief executive of
> Vector, pins his hopes on a product instead of a financial strategy. In
> order to get there, however, LeBow had to cut a life-saving deal to settle
> a 1995 Medicaid lawsuit against tobacco manufacturers, and he had to burn
> furniture, selling all of Vector's Russian assets, to keep going. Vector
> recently caught the attention of corporate raider Carl Icahn, who pumped
> \$48 million into Vector in August, increasing his share to 22 percent. > > Now,
Vector has hired a former top marketing executive from market leader

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> Philip Morris and is putting a \$75 million campaign into gear, with a
 > market launch planned for the end of this month. > > But Vector is still facing
 challenges. LeBow thinks he can overcome
 > technical hurdles, eliminating remaining cigarette carcinogens from Omni.
 > But, according to LeBow, a bigger hurdle are competitors' animosities. And
 > then there are long-term business risks, including the potential for
 > litigation. > > Liggett scientists discovered the palladium process 30 years ago in
 top
 > secret research dubbed Project XA. Liggett attorneys killed Project XA
 > shortly thereafter, terrified it could be prima facie evidence Liggett
 > knew cigarettes cause cancer. > > After buying Liggett in 1986, LeBow revived the
 project - after learning
 > about XA from a secretary. "We found Project XA cigarettes in cold
 > storage," he told the Daily Business Review in an interview. > > By now, he
 estimates, safe cigarette research has cost him \$106 million.
 > "It's the right thing to do," says LeBow, 62. > > "It may open us to legal liability
 - I don't care. I tell my people I
 > don't want to hear that," he says. > > LeBow said that he dismissed attempts by his
 lawyers to discuss the legal
 > ramifications of creating a truly safe cigarette. > > LeBow cites the nastiest
 hurdle for Omni: "Our competitors are doing
 > everything they can to keep Omnis off the shelves, partly to protect their
 > market share, partly it's personal," he says. "They hate me," he adds,
 > flaunting his tobacco industry maverick/traitor status like a badge of
 > honor. > > If the launch works, Liggett, the smallest of the six major U.S. tobacco
 > companies with a 1 percent market share, has a lot to gain. Analysts think
 > Omni may help Vector to at least double its revenues. In 2000, the company
 > posted revenues of \$739 million. > > But there still are a couple of snags.
 Competitor Philip Morris Co. told
 > growers in North Carolina, Kentucky and Argentina that it will boycott any
 > farmer who planted even a tiny plot of genetically modified tobacco. > > "We're not
 blocking the product, but the growers are aware of our
 > concerns," said Ellen Merlo, Philip Morris senior vice president of
 > corporate affairs. But, she adds, "even a small percentage of genetically
 > modified tobacco can contaminate a whole crop." > > Asked about evidence, she could
 not cite a scientific study. > > "We feel genetically altered tobacco needs to be
 segregated all through
 > the supply chain," said Mike Pfeil, senior vice president of
 > communications for Philip Morris. "In Argentina, I believe, the government
 > ultimately decided all the genetically modified tobacco had to be
 > destroyed." > > Liggett circumvented the problem by convincing Pennsylvania Amish
 farmers
 > to grow 3,000 acres of genetically modified tobacco, enough for 2 billion
 > Omnis. > > However, LeBow is more enraged about another assault. "When you use
 > tobacco, you have to remove stems," he explains. "There are only 20
 > stemeries in the world that do this very specialized, technical work." > > He says
 his competitors also threatened to boycott any stemery he used. "I
 > finally had to build my own stemery in North Carolina. Cost me \$15
 > million." > > To be sure, LeBow is not new to controversy. He made industry history
 and
 > enemies with the 1995 deal that allowed Liggett to settle lawsuits from 40
 > state attorney generals. In return, LeBow admitted that nicotine is
 > addictive and that smoking causes cancer. He cooperated with Justice
 > Department investigations into cigarette marketing. It was a fatal break
 > with his competitors' legal strategy of mass denial. > > The move was especially
 shocking for Philip Morris, which was paying
 > Liggett's \$8 million legal fees that year to maintain a united front. > > Investors
 and analysts so far are optimistic about Omni. Since Vector
 > announced in February that it had patented a genetically modified,
 > nicotine-free tobacco variety, its stock price more than doubled to a

> 52-week high of \$46.46 on Oct. 4. > > But the shares traded at \$43.05 midday Wednesday, more than \$3 down from
> its 52-week high.
> "It's just investors taking a little money off the table because Vector's
> had such a good run," said Bonnie Herzog, tobacco analyst with Credit
> Suisse First Boston, about the recent drop. > > "I don't expect Liggett to be the
next Marlboro," she says. But, she adds,
> "The tobacco industry hasn't seen a new product in years, and unlike other
> attempts at safe cigarettes, Ben's burns and tastes like real tobacco. And
> the fact that Carl Icahn stepped up to the plate reassured a lot of
> investors." > > Last month LeBow hired a Philip Morris marketing veteran, James
Taylor,
> who spent 12 years shaping the macho, risk-loving Marlboro smoker image.
> Taylor had left Philip Morris to join a dot-com because, according to
> LeBow, he was disgusted with the tobacco industry's deceptions. > > Omni's \$75
million to \$100 million marketing campaign's slogan is "Premium
> Taste, Less Carcinogens." The \$29 per carton cigarettes are pitched to
> smokers haunted by life's fragility with what sounds like gonzo honesty. > > "They
can still give you emphysema and heart trouble," LeBow says. "But
> we're working on that. We think we can fix that." > > FDA discussions > > It's a
long road still to perfect safety. LeBow hired a research team at
> North Carolina State University, where the genetically modified tobacco
> was created. > > LeBow is negotiating with the Food and Drug Administration to sell
Omni
> Nicotine Free as a stop-smoking aid. But in Vector's own six-week study
> with 60 smokers, all went back to their nicotine-soaked brands. "Six weeks
> isn't enough time," says LeBow, who quit smoking cold turkey in six weeks
> decades ago. > > LeBow blames the competition for the study's deficits. He says the
boycott
> threats meant there was only enough genetically modified tobacco for one
> small-group study. > > LeBow is undaunted. "Nicotine patches don't work," he says.
"Omni will
> work because the ritual of smoking is more important than the habit." > > The
competition has failed miserably because it didn't consider the ritual
> aspect, LeBow suggests. His nemesis, Philip Morris, created a reduced-risk
> cigarette kit a few years ago that looked like a crack-pipe kazoo. > > A digital
display tracked a smoker's puffs. Focus groups detested it as a
> bizarre machine. Tobacco ads always sold cigarettes as a crucial prop for
> glamorous or dangerous poses, the camaraderie of bumming enveloping smoke.
> > "Nicotine hooks you; the ritual keeps you," LeBow says. "Omni keep the
> ritual." > > Meanwhile, there's also a technical obstacle overseas for Omni.
> Financially desperate Russia produces 66 percent of the world's palladium
> and is
> hoarding it. This summer, the price for an ounce shot to \$1,100. (Platinum
> was only \$645.) > > But LeBow now says Liggett has created a palladium substitute
for its
> process. > > LeBow would not reveal any more details about the process. Says LeBow:
"We
> don't need to stockpile like the U.S. car manufacturers." > > The palladium process
destroys polycyclic aromatic hydrocarbons (PAH), the
> carcinogens that form behind the burning tip. Before the FDA allows him to
> drop a warning label from packages, LeBow knows he must eliminate
> cigarettes' other carcinogenic compounds, like nitrosamines, in tobacco
> smoke. "We got them down by 20 to 40 percent," he says. > > He says Liggett's goal
of selling only safe cigarettes is obtainable in
> his lifetime. "From 1993 to 1998, we had one scientist. Philip Morris had
> 600. > > "What the hell have they been doing all this time?" he asks. > > Yet he
wavers when asked whether the tobacco industry will exist in 30
> years. > > "I don't know if cigarette manufacturers can stay in business if they
> don't sell to kids," he muses. "I was 16 when I started smoking. Almost no

> one starts as an adult." > > And he won't predict how big Liggett's market share
will be with a
> carcinogen-free Omni. "I refuse to dream," he says flatly.

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